

Tortoise QuickTake

Credit Podcast



Dec. 18, 2018

Narrator: Welcome to the Tortoise Quick Take podcast. Thank you for joining us. Today, senior members of Tortoise provides a timely update on trending topics in the market.

Hi, I'm Graham Allen, Senior Portfolio

In Parliament, the British Prime Minister emphatically ruled out another referendum saying that a second vote would be divisive and not decisive. So come what May, pun intended, there will be no second referendum on Brexit, at least on her watch. This increases the chances that Brexit will happen.

But the state of Brexit is fraught. In the words of Bernie Taupin, "It's a sad, sad situation, and it's getting more and more absurd."

In all the confusion and drama of the current situation it may be worth taking a step back to see if a more high level assessment could give us some clarity. Determining any outcome is difficult as there are so many conflicted interested parties combined with a large number of variables. This is complicated by the fact that the factions of two major parties, who originally voted to leave, have probably changed their minds but are not publically saying so.

So what do we know for sure? We know that on June 23rd, 2016 a referendum on leaving the European Union was put to the British people. The choice was binary, and the voters told it would be the final decision. The vote was 52% to 48% to leave. Despite statements to the contrary by both sides, there is little evidence that there has been a significant shift in the voter's original stances. Although many are now calling for a second referendum, this now seems highly unlikely under existing circumstances. Her leadership under pressure, Theresa May has said she will not seek another term. So her legacy may now best be served by delivering this historic event to the country, despite her earlier vote to remain. If nothing else, her recent comments underscore the importance she places on the democratic sanctity of the 2016 vote.

Her recent comments in Parliament even prompted statements of support for her leadership from some hardline Brexiteers who voted against her in the no confidence vote. Given this, there is unlikely to be a change of her leadership any time soon, not the least of reasons being there are no real obvious candidates to replace her. Labour's call for another vote of confidence will not succeed, even if it gets to a vote.

While the Prime Minister doggedly continues to push a deal which she knows is dead on arrival in its present form, there are signs that the U.K. government is finally coming to terms with reality. Certain contingent provisions are being put into place for a no deal exit, including approval of a plan by the Cabinet and specific no deal funding.

Of course, most of the recent focus has been on the embarrassing chaos in the British Parliament, giving fuel to the Remainers to pressure for any event that could stop the Brexit process. But much of the chaos has been caused by the unwillingness of the EU to shift in the negotiations with Theresa May from an agreement they know she cannot get through Parliament.

In the bigger picture, examining the motives of the EU, as represented by Brussels becomes critical to understanding what may happen. On the face of it, the EU actually doesn't hold a strong bargaining position, although this is rarely acknowledged. In addition to the embarrassment that Brexit represented in the first place, the EU has the problem of an estimated €90 billion trade surplus with the UK, and receives a net positive contribution of approximately €10 billion to the EU budget. The cost of a hard UK exit would therefore have a far greater negative economic impact on the EU than the U.K., not to mention an existential threat to the European Union from having a core member leave.

It's logical to assume therefore, that the negotiating stance of Brussels at this stage is motivated by a desire to see Brexit not occur, and it's a fair assessment that given the chaos surrounding the U.K. government's very public internal squirming, it

appears to be working. At the very least Brussels wants to make the process of leaving as publicly difficult and embarrassing as possible for the U.K. if they are unable to stop it altogether. Knowing that time is running out, why would do they do anything different, at least for now?

The status quo is unlikely to last as the stark reality of a hard Brexit approaches. This may lead to a more pragmatic approach from all parties as the deadline gets closer and the cost to both sides of a hard exit crystalize. Given that Theresa May now seems adamant that Brexit will occur, the desire for a negotiated deal, tolerable to her own party will grow even among the hardliners.

From Brussels's perspective as the deadline approaches, the EU will increasingly face internal backlash from the European industries most affected by a 'no deal' exit, most notably the French wine and the German car industries to name two. The internal chaos on display in the U.K. could easily transfer to Europe as a whole, except in Europe's case, the disruption may spread to affect wider frustrations. Politicians coping with rising anti-EU sentiment within the Union will also not welcome the chaos of a hard Brexit, as it could be viewed as another example of an EU establishment insensitive to the needs of the people. Recent 'yellow vest' protests in France and Belgium along with the Italian budget impasse are already indicative of dissatisfaction with the political management of the Union. The underlying causes of the recent unrest are not improving and a chaotic divorce from the U.K. will almost certainly exacerbate a slowing European economy and expose the worsening economic fissures, one cause of the frustration in the first place. This puts enormous pressure on the EU to ultimately come to a workable divorce settlement with the U.K.

However before this occurs, it would be wise to heed a high surf warning, as things could get choppy between now and then.

We hope you have enjoyed this podcast. Happy Holidays.

Thank you for joining us. And stay tuned for our next cast. Have topics you want covered or other feedback to share? Write us at info@tortoiseadvisors.com.

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